WHITE PAPER

Boost Your Working Capital with EDC's Export Guarantees

Every exporter knows that it's hard to succeed in foreign trade without an adequate supply of working capital. Most exporting companies go to their banks to meet this need, but the risks of international trade combined with your own financial position can reduce your lender's willingness to support your foreign sales or operations. This white paper looks at how EDC's Export Guarantee Program (EGP) can help you overcome such barriers, enhance your partnership with your bank and furnish the cash to grow your international sales.

TABLE OF CONTENTS

INTRODUCTION

If you've been an exporter for any length of time, you'll know that working capital is a vitally important tool for driving and sustaining your company's growth abroad. With enough cash, you can support your immediate and long-term plans, expand into new markets and take on larger contracts. With too little, your growth will be sluggish or nonexistent.

Even if you're an experienced exporter with a helpful lender, however, you may eventually find that you're looking for more cash than your bank is willing to provide. Before it will extend the incremental financing you need, the bank may consequently require a third-party guarantee to protect it if you default on repayment.

It's in situations like these that EDC's EGP can come to the rescue. By providing your bank with up to CAD 10 million in total guarantees, the EGP can give it the confidence it needs to furnish you with more financing for your business. And because the EGP is so flexible, it can support more than 10 different financing scenarios that can range from bigger operating lines to assistance with your international investments.

APPLYING FOR AN EGP GUARANTEE

You and your bank will need to work together to apply for a guarantee under the EGP. To do so, your bank must be willing to set up a loan for your company. For your part, you'll need to provide financial statements to support the application. Not all account managers are familiar with the EGP, though, so you may have to tell them about it and suggest they contact EDC to start the wheels turning.

MORE CASH FOR YOUR OPERATING LINE

The EGP offers multiple approaches to expanding your access to cash, as the following scenarios illustrate.

- **Increasing your general operating line**

  Your company sells most of its production to buyers in the United States. Your U.S. sales are increasing very quickly and you've secured footholds in Asia as well. You need more working capital to finance all this growth, so you ask your bank to increase your operating line.

  Your bank, however, is uneasy about the risk associated with your company's rapid expansion and is unwilling to extend the full amount you need. To solve the problem, your account manager works with EDC to arrange an EGP guarantee that will cover up to 75 per cent of the amount of your new line. With the guarantee in place, the bank carries only 25 per cent of the total risk. It can now increase your operating line so you can proceed with your plans for growth.

- **Margining your foreign receivables**

  Your company has been experiencing steady international growth and now you need an infusion of working capital. To obtain it, you ask your bank for a new operating line, to be margined against your foreign accounts receivable (ARs).

  Your bank, however, is reluctant to margin non-Canadian ARs. Knowing this, your account manager suggests turning to EDC, which can issue an EGP guarantee against the value of your foreign receivables. The guarantee will cover 65 per cent of the risk of the new operating line, leaving the bank with an acceptable risk of 35 per cent. The bank can now margin your foreign AR, allowing you to expand into new markets.

- **Margining your foreign inventory**

  Because of your European buyers' tight delivery demands, your company maintains a large inventory of goods in Spain. You need more working capital, so you've asked your bank to increase your operating line by margining this overseas inventory. The bank already margins 50 per cent of your domestic inventory, so it seems a reasonable request.

  Unfortunately, your bank's lending guidelines prohibit margining foreign inventory, so you need another solution. It comes in the form of an EGP guarantee, which will allow the bank to margin the overseas inventory at the same level as your domestic inventory. With the guarantee in place, the bank increases your line and you can begin expanding your foreign sales.

- **Margining your R&D credits**

  Your company exports most of its production and maintains a vigorous R&D department to sustain its growth. You need additional working capital for your R&D, so you ask your bank for a new operating line. This, you hope, could be margined against your end-of-year tax credits from the federal government's Scientific Research and Experimental Development (SR&ED) tax incentive program.

  However, the bank is unwilling to extend the full amount, since it considers such margining to be too risky. Fortunately, the EGP offers a solution – it can guarantee 75 per cent of the sum you've requested, leaving the bank with only 25 per cent of the risk. This allows the bank to set up the new operating line so you can carry out your R&D plans.

SUPPORT FOR YOUR FOREIGN SALES

The EGP can be a vital part of financing your foreign sales, whether for one contract or several. The following scenarios show why.

- **Financing single export contracts**

  Your company has just signed a large, one-time contract with a Chinese buyer, and you've asked your bank for a separate credit line to finance the contract's upfront costs. The line would only be needed until you receive your buyer's final payment.

  Unfortunately, the bank can't extend the total amount needed, since it already has considerable exposure to your company. To solve the problem, the bank suggests an EGP guarantee that will secure 75 per cent of the line needed for the contract. With the guarantee in place, and with its own risk reduced to 25 per cent, the bank will be able to finance your contract's upfront costs until you've received full payment.

- **Financing multiple export contracts**

  You're a new exporter and have just secured your first deal in the United States, plus commitments for two more U.S. contracts over the next year. As a result, you've asked your bank to set up a facility to finance the upfront costs of these contracts, plus the costs of any additional contracts you might sign over the next 12 months.

  You've asked the bank to use your product inventory to secure the increase, but there's a problem – your products are highly specialized and have little value as security, so your bank can extend only a quarter of what you're asking. The EGP, however, can provide a 75 per cent guarantee on a revolving credit line that will meet your needs for a year. With this guarantee in place, the bank can cover the remaining 25 per cent of the risk, and will be able to extend the full amount you've requested.

- **Financing your indirect exports**

  Your company manufactures a line of components that it sells to various equipment manufacturers across Canada. You've just contracted to supply one of these manufacturers with parts for its products. Because the Canadian manufacturer sells these assembled products abroad, your sales under the contract fall into the category of indirect exports.

  To finance production related to the contract, you ask your bank for a contract-related financing facility, which you'll need until you receive final payment from the Canadian manufacturer. The bank is uncomfortable with this, however, because your components are specialized and will also leave Canada before you get paid. The solution is an EGP guarantee that will secure 75 per cent of the credit provided by the bank. The remaining 25 per cent is within the bank's credit guidelines, so it agrees to provide up to 100 per cent of the cash you need for fulfilling the contract.

- **Financing term loans for your capital expenditures**

  Your sales abroad are increasing rapidly. You need a capital expenditures loan of several million dollars so you can buy new machinery to meet the demand, but your bank is uneasy about increasing its exposure to your company. And if it won't extend the full amount of the loan, you'll have to cancel your expansion plans.

  Once your bank and EDC arrange an EGP guarantee, however, you're back on track. The guarantee covers 75 per cent of the loan you need and the balance is within the bank's exposure limit. The bank issues the full amount of the loan and you can begin tendering for your new equipment.

- **Helping your suppliers get the financing they need**

  Your company has signed a large U.S. contract to supply production equipment and you need a large quantity of specialized components to assemble the machinery. However, your component supplier needs financing to fulfil your order, but it can't obtain increased credit from its bank. The EGP provides the solution by securing 75 per cent of the necessary loan from the supplier's bank, and the supplier can now provide the components you need for your U.S. contract.

SUPPORT FOR YOUR FOREIGN INVESTMENTS

If you want to acquire a company abroad, or obtain financial support for an existing affiliate, the EGP may be able to help. The following scenarios show how this can work.

- **Support for your acquisitions abroad**

  Your company has decided to acquire a U.S. firm in order to expand into the United States. You'll need a bank loan to help with the purchase, but the amount would put your debt-to-equity ratio beyond your bank's upper limit.

  With the acquisition in jeopardy, you and your bank turn to the EGP – which can support investments outside Canada – and set up a guarantee that secures up to 100 per cent of the loan for a period of three years. Once the loan is in place, you can begin the process of acquiring the U.S. company.

- **Support for your foreign affiliate's operating line**

  As part of your company's global expansion plans, you've acquired an Australian manufacturing firm. Its financing comes from an Australian bank and you've asked this bank to set up an operating line of $1 million for your new acquisition. But the bank will do so only if you provide security in the form of a standby letter of credit (SLC) for $1 million. Your Canadian bank can issue the SLC, but it will require $1 million in collateral to do so. It can take this cash from your current operating line, but this will severely erode the working capital you need for your Canadian operations.

  The EGP turns out to be the answer. It provides a guarantee so your Canadian bank can issue the SLC to the Australian bank without pulling the collateral from your operating line. With the SLC in place, the Australian bank can set up your Australian affiliate's operating line, while your Canadian operations will retain all the working capital they need.

COVERAGE

The value of an EGP guarantee can vary depending on the credit strength of your company and the security associated with the loan. EDC's total exposure under one or multiple EGP guarantees in support of your business cannot exceed CAD 10 million.

In general, coverage is as follows:

- For financing of domestic assets, guarantees can be up to 75 per cent.
- Individual credit facilities may be guaranteed up to 90 per cent, providing that the guaranteed amount is less than $500,000 and the financial institution has other exposure with the customer.
- Up to 100 per cent coverage is possible for the financing of qualifying foreign assets. Typical foreign financing scenarios include a foreign affiliate's working capital, a foreign affiliate's capital expenditures, foreign-domiciled inventory owned by you or your foreign affiliate, or an operating line for your foreign affiliate.

QUESTIONS?

Call 1-866-838-0267 weekdays 8 am to 4 pm EST.
Complete an online **inquiry** form.

Ce document est également disponible en français.

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